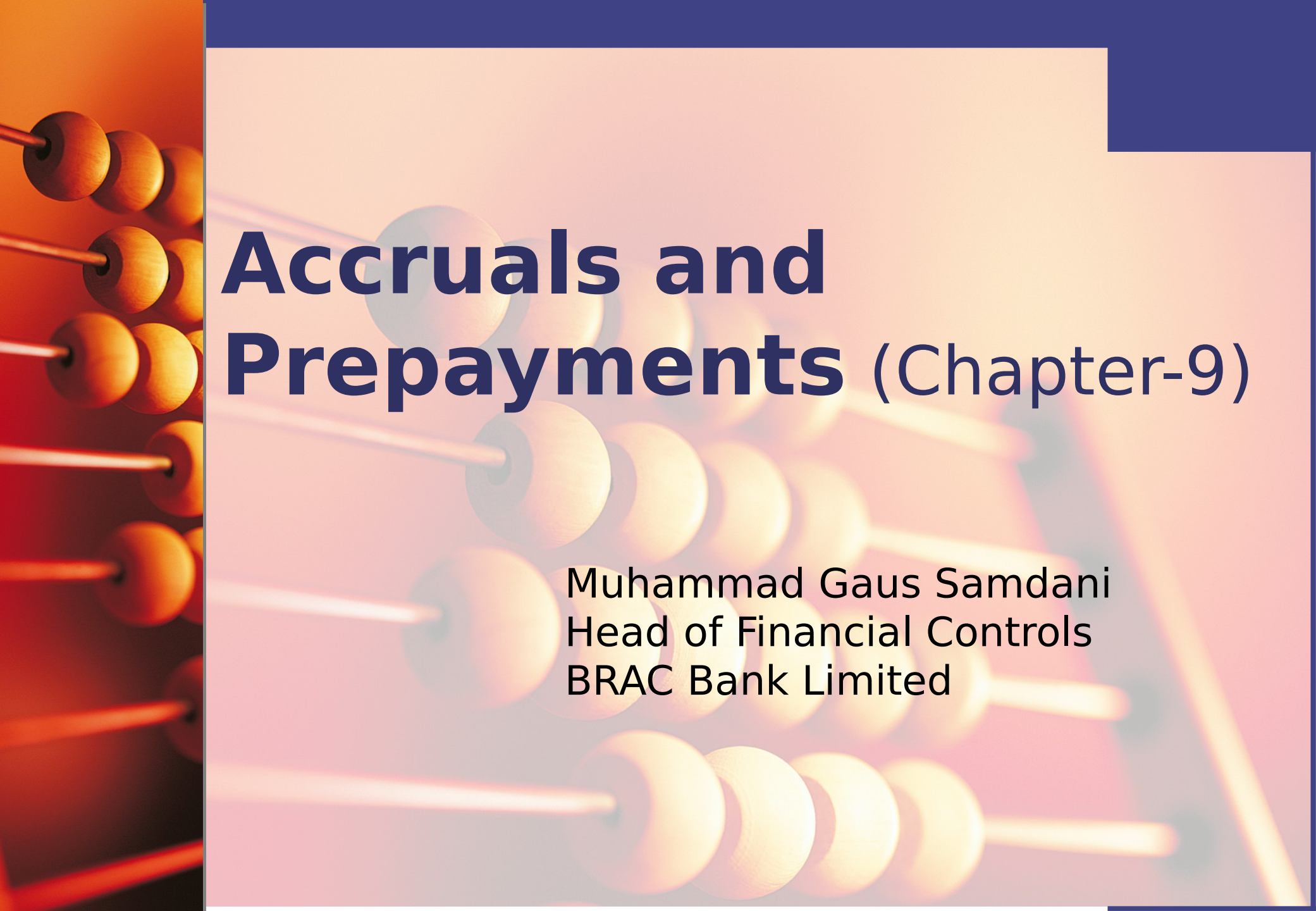
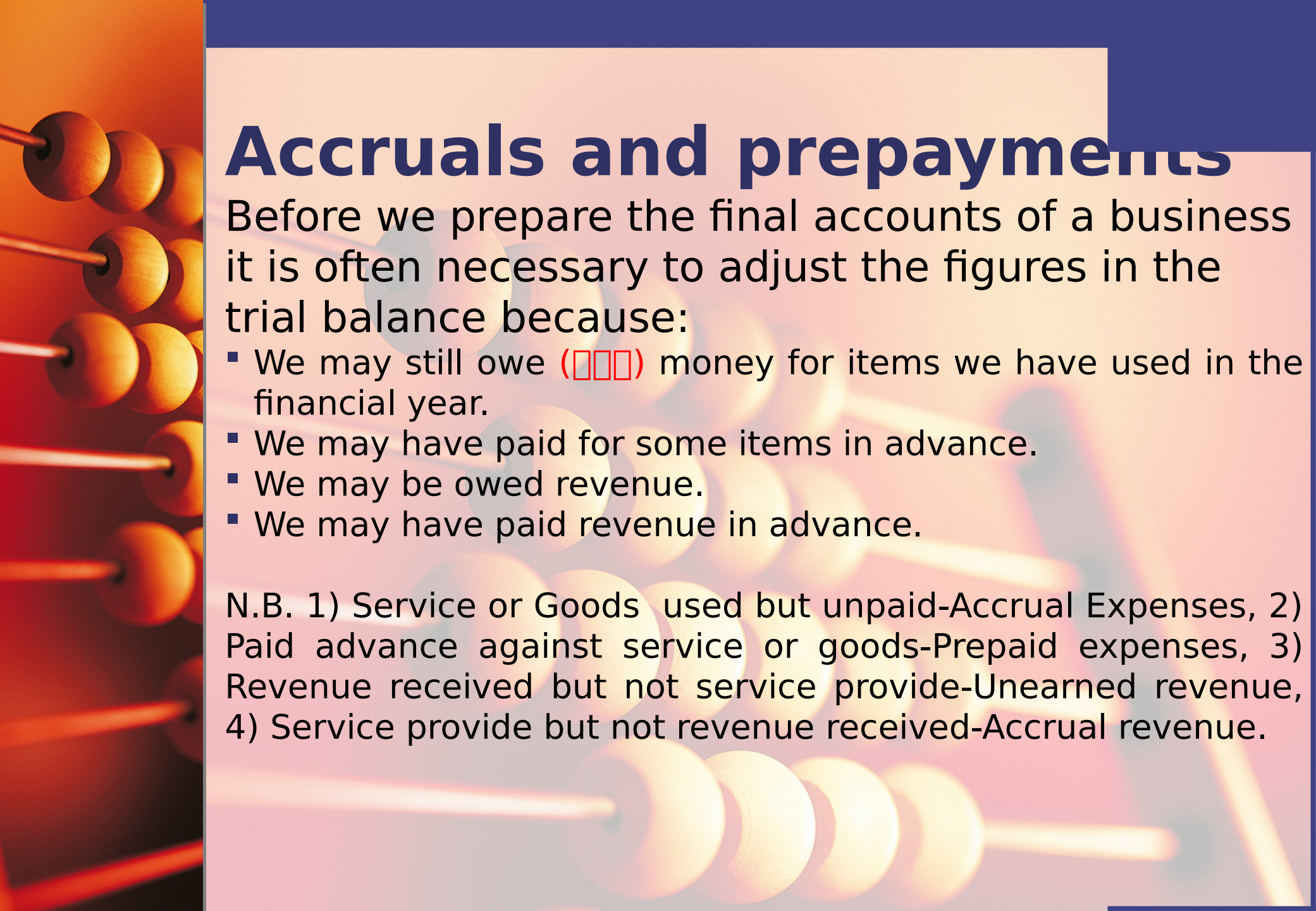




Accruals and Prepayments (Chapter-9)

Muhammad Gaus Samdani
Head of Financial Controls
BRAC Bank Limited

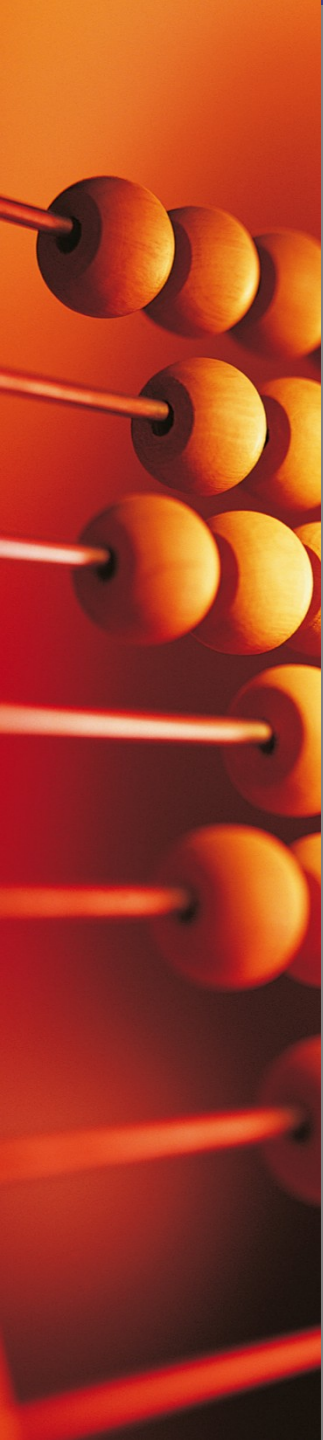


Accruals and prepayments

Before we prepare the final accounts of a business it is often necessary to adjust the figures in the trial balance because:

- We may still owe (□□□) money for items we have used in the financial year.
- We may have paid for some items in advance.
- We may be owed revenue.
- We may have paid revenue in advance.

N.B. 1) Service or Goods used but unpaid-Accrual Expenses, 2) Paid advance against service or goods-Prepaid expenses, 3) Revenue received but not service provide-Unearned revenue, 4) Service provide but not revenue received-Accrual revenue.

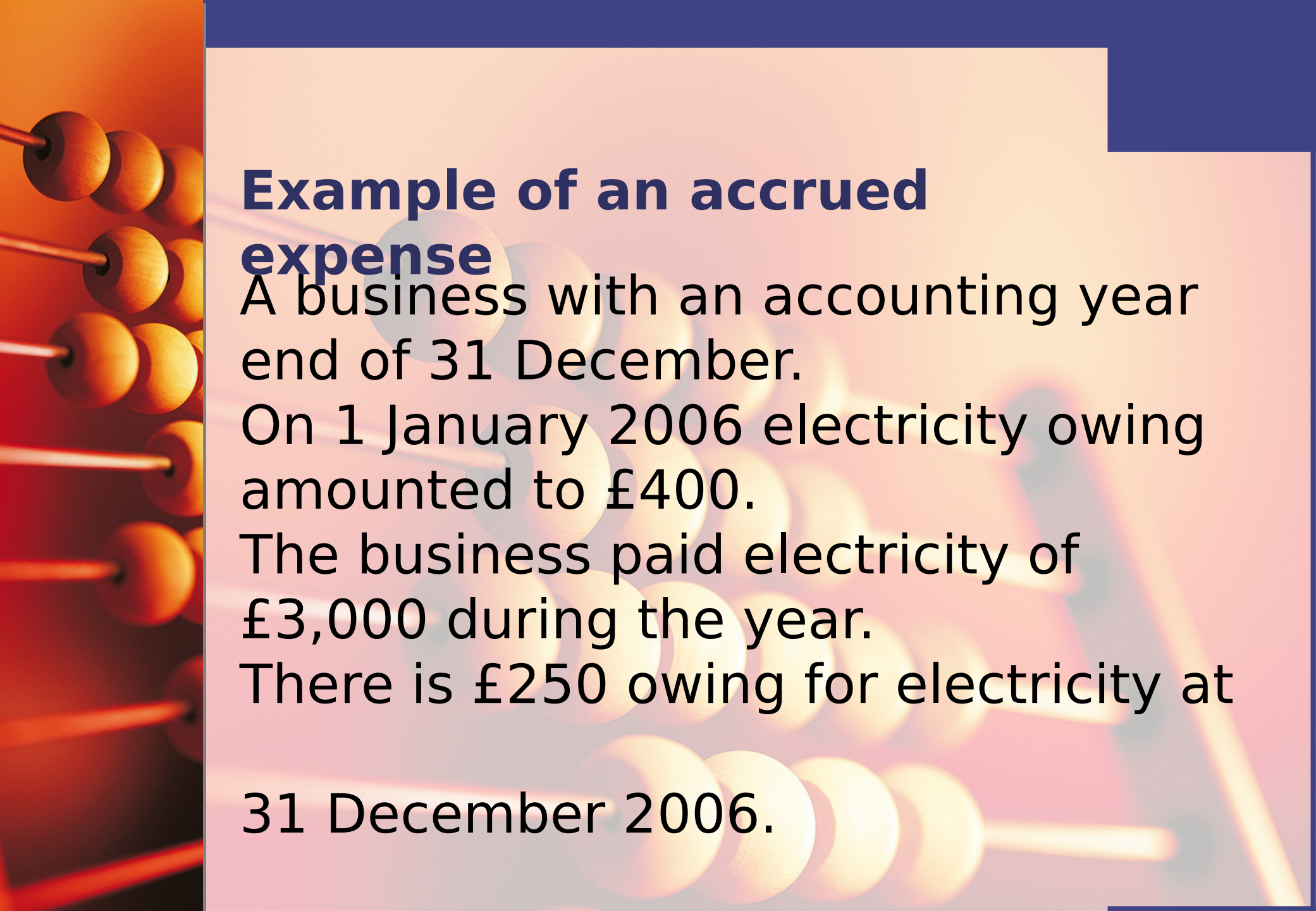


What are accruals?

An accrual (expense, liability) is an estimate of money that is owed (expense), but which has not yet been paid.

What are prepayments?

A prepayment is a payment made in advance of the current period.



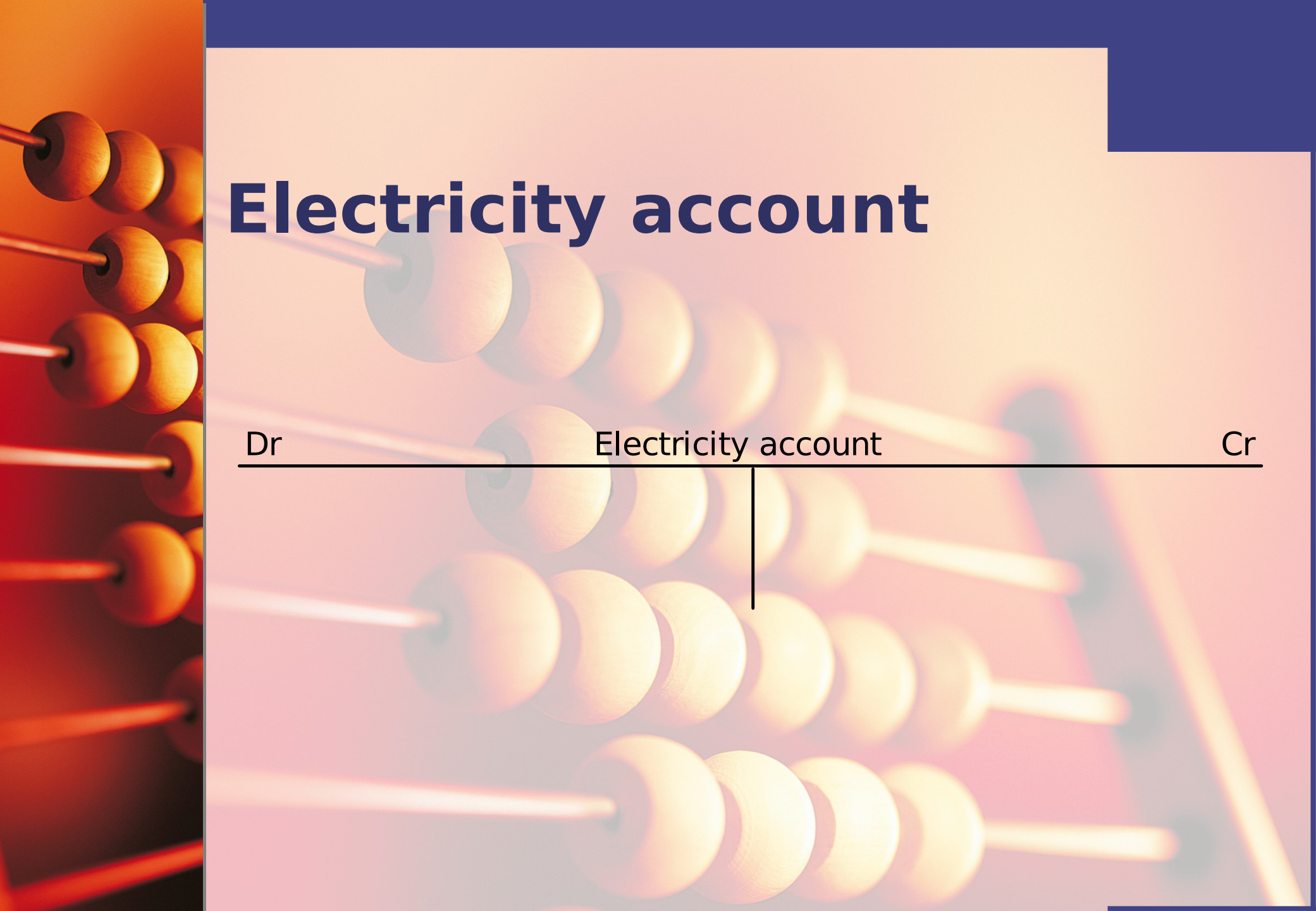
Example of an accrued expense

A business with an accounting year end of 31 December.

On 1 January 2006 electricity owing amounted to £400.

The business paid electricity of £3,000 during the year.

There is £250 owing for electricity at 31 December 2006.

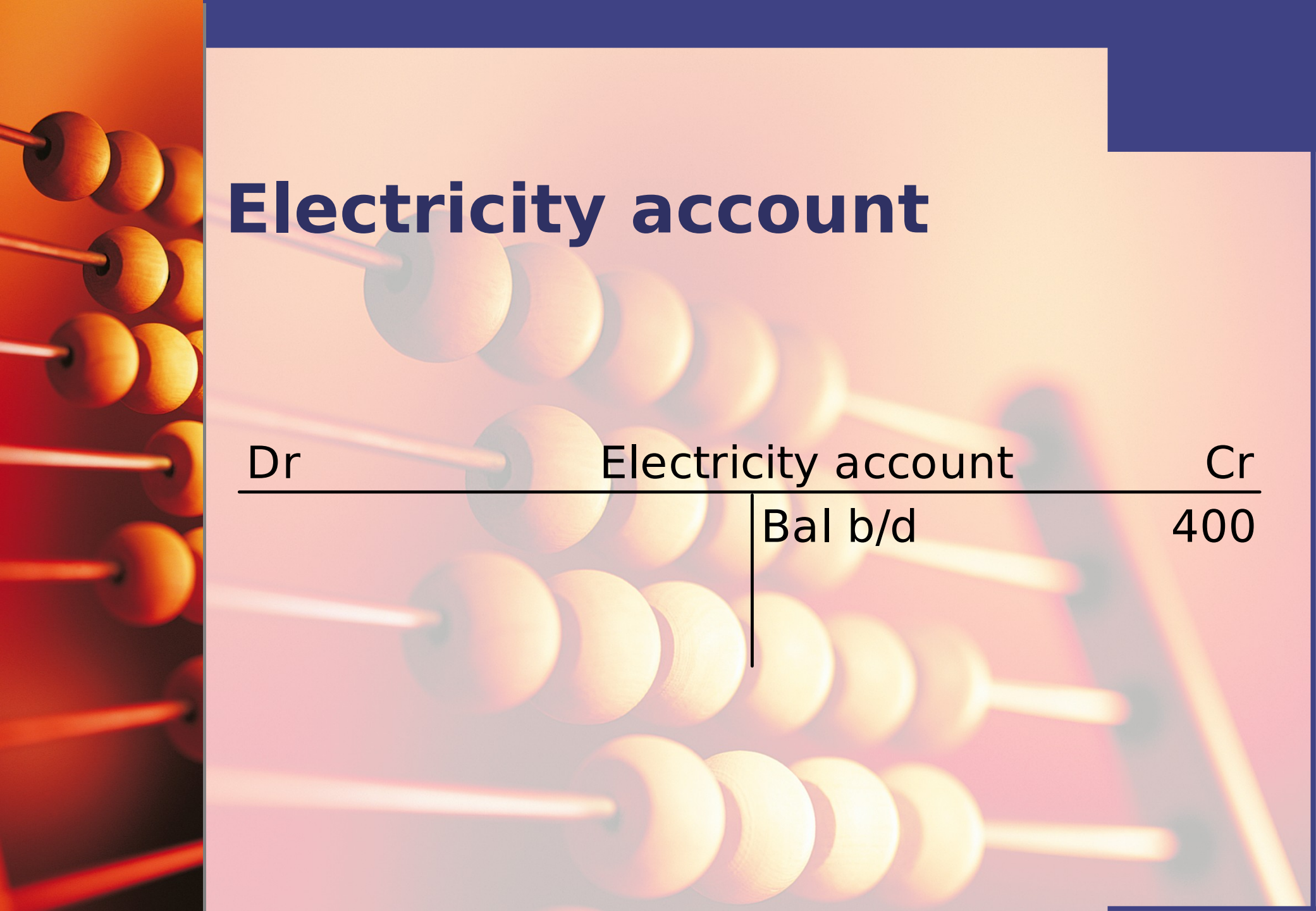


Electricity account

Dr

Electricity account

Cr



Electricity account

Dr	Electricity account	Cr
	Bal b/d	400

Electricity account

Dr	Electricity account	Cr
Bank	3,000	Bal b/d 400

Electricity account

Dr	Electricity account		Cr
Bank	3,000	Bal b/d	400
Bal c/d	250		

Electricity account

Dr	Electricity account	Cr
Bank	3,000	Bal b/d 400
Bal c/d	250	Profit and loss 2,850
	<u>3,250</u>	<u>3,250</u>

**Profit and loss account for the year ended
31 December 2006 (extract)**

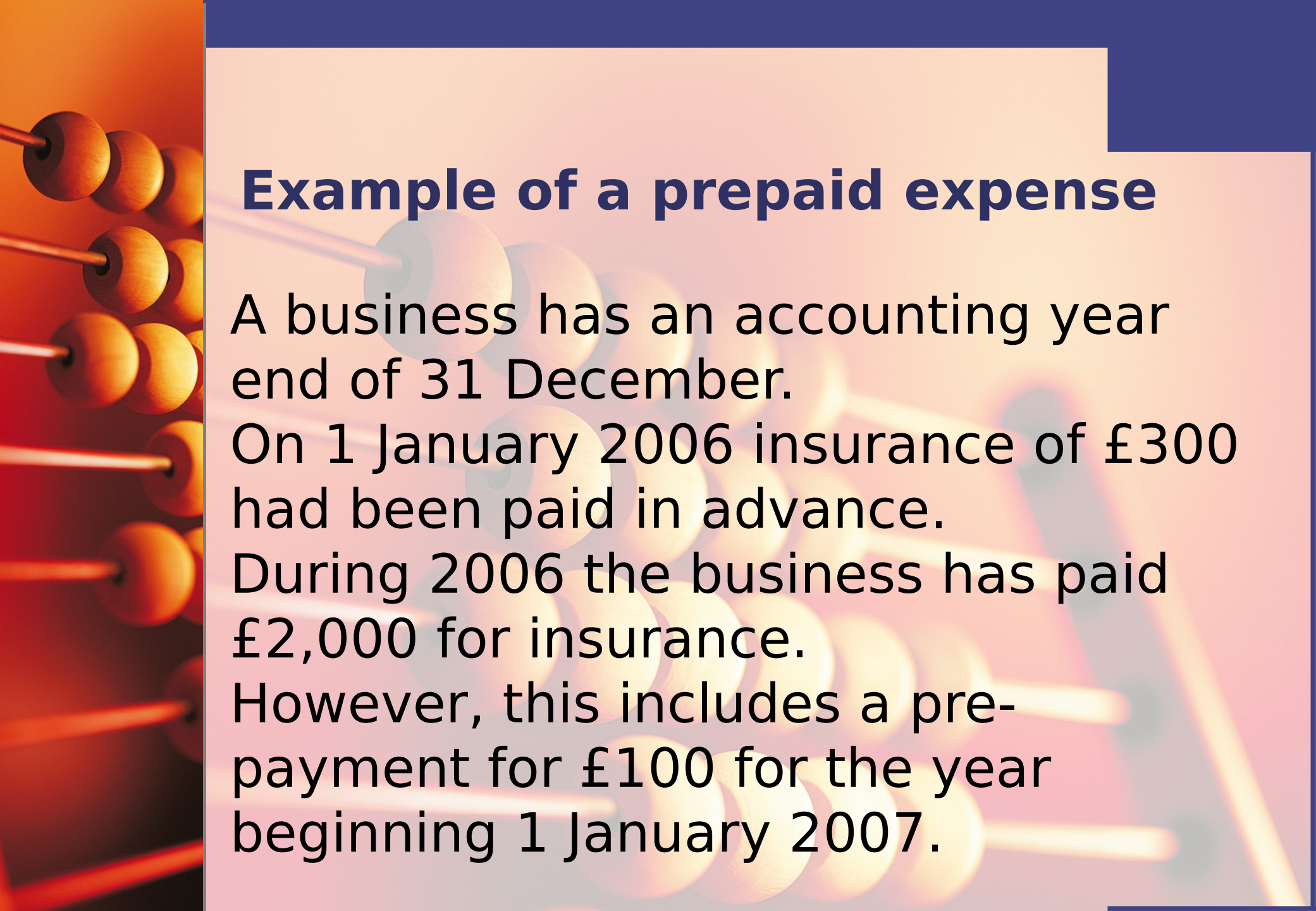
Less expenses

Electricity	2,850
-------------	-------

**Balance sheet as at 31 December 2006
(extract)**

Current liabilities

Electricity accrued	250
---------------------	-----



Example of a prepaid expense

A business has an accounting year end of 31 December.

On 1 January 2006 insurance of £300 had been paid in advance.

During 2006 the business has paid £2,000 for insurance.

However, this includes a pre-payment for £100 for the year beginning 1 January 2007.

Insurance account

Dr	Insurance account	Cr
----	-------------------	----

Insurance account

Dr	Insurance account	Cr
Bal b/d	300	

Insurance account

Dr	Insurance account	Cr
Bal b/d	300	
Bank	2,000	

Insurance account

Dr	Insurance account	Cr
Bal b/d	300	
Bank	2,000	Bal c/d 100

Insurance account

Dr	Insurance account		Cr
Bal b/d	300	Profit and loss	2,200
Bank	2,000	Bal c/d	100
	<u>2,300</u>		<u>2,300</u>

**Profit and loss account for the year ended
31 December 2006 (extract)**

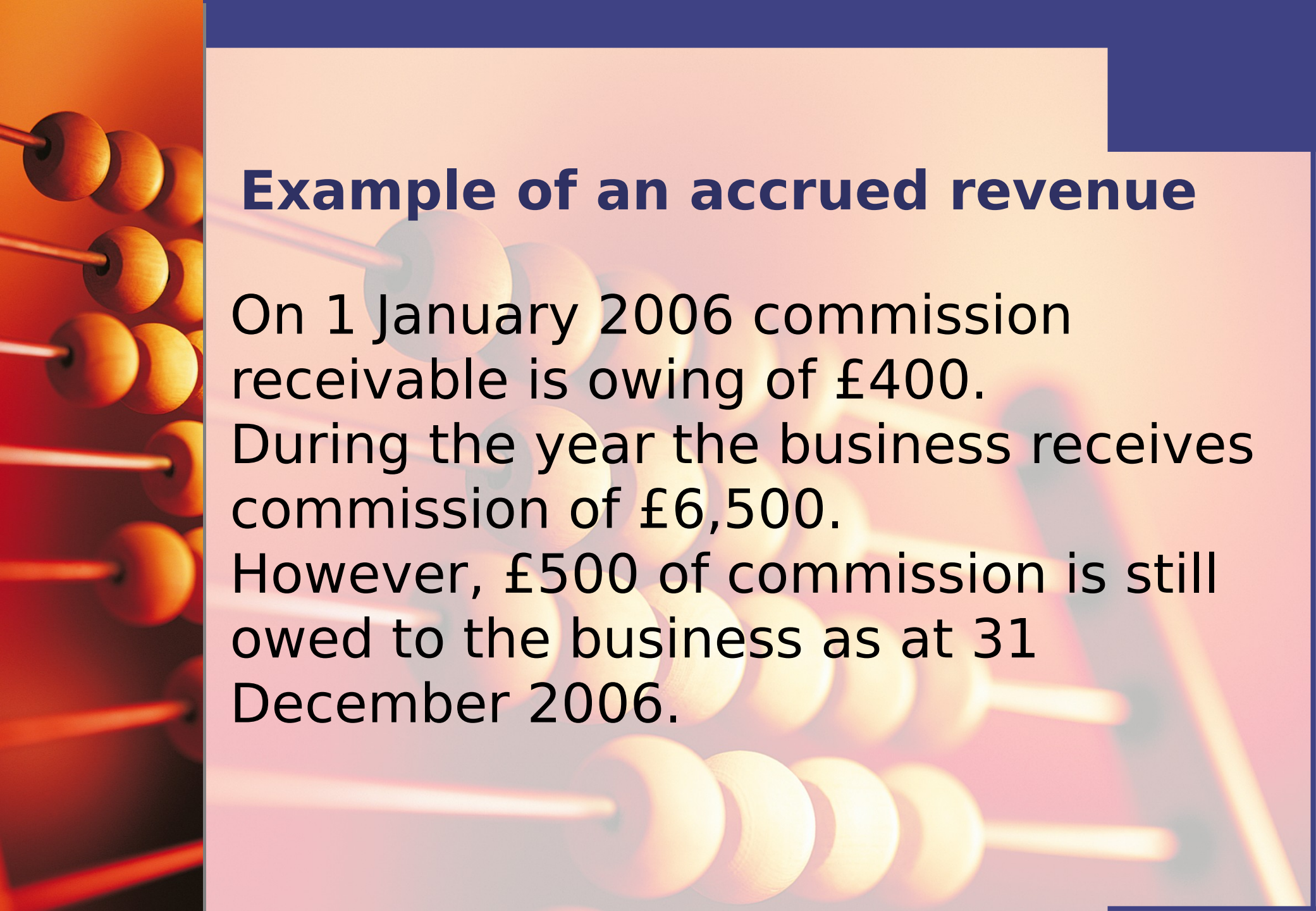
Less expenses

Insurance	2,200
-----------	-------

**Balance sheet as at 31 December 2006
(extract)**

Current assets

Insurance prepaid	100
-------------------	-----



Example of an accrued revenue

On 1 January 2006 commission receivable is owing of £400.

During the year the business receives commission of £6,500.

However, £500 of commission is still owed to the business as at 31 December 2006.

Commission received

Dr	Commission received	Cr
----	---------------------	----

Commission received

Dr	Commission received	Cr
Bal b/d	400	

Commission received

Dr	Commission received	Cr
Bal b/d	400	Bank 6,500

Commission received

Dr	Commission received	Cr
Bal b/d	400	Bank 6,500
		Bal c/d 500

Commission received

Dr	Commission received		Cr
Bal b/d	400	Bank	6,500
Profit and Loss	6,600	Bal c/d	500
	<u>7,000</u>		<u>7,000</u>

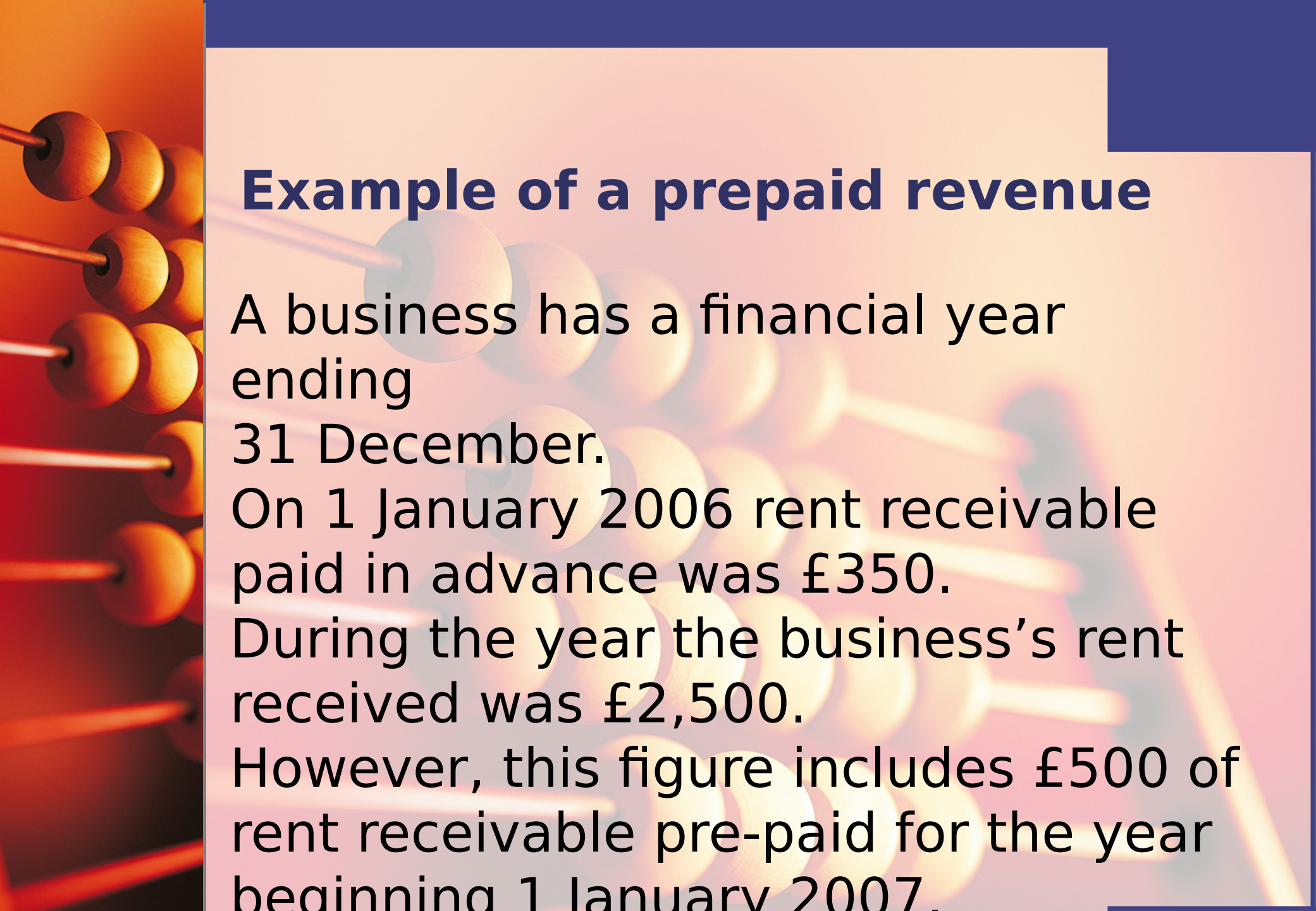
**Profit and loss account for the year ended
31 December 2006 (extract)**

Gross profit	xxx
Add commission received	6,600

**Balance sheet as at 31 December 2006
(extract)**

Current assets

Accrued commission receivable	500
-------------------------------	-----



Example of a prepaid revenue

A business has a financial year ending 31 December.

On 1 January 2006 rent receivable paid in advance was £350.

During the year the business's rent received was £2,500.

However, this figure includes £500 of rent receivable pre-paid for the year beginning 1 January 2007.

Rent received

Dr	Rent received	Cr

Rent received

Dr	Rent received	Cr
	Bal b/d	350

Rent received

Dr	Rent received	Cr
	Bal b/d	350
	Bank	2,500

Rent received

Dr	Rent received	Cr
		Bal b/d 350
Bal c/d 500		Bank 2,500

Rent received

Dr	Rent received	Cr
Profit and loss	2,350	Bal b/d 350
Bal c/d	500	Bank 2,500
	<u>2,850</u>	<u>2,850</u>

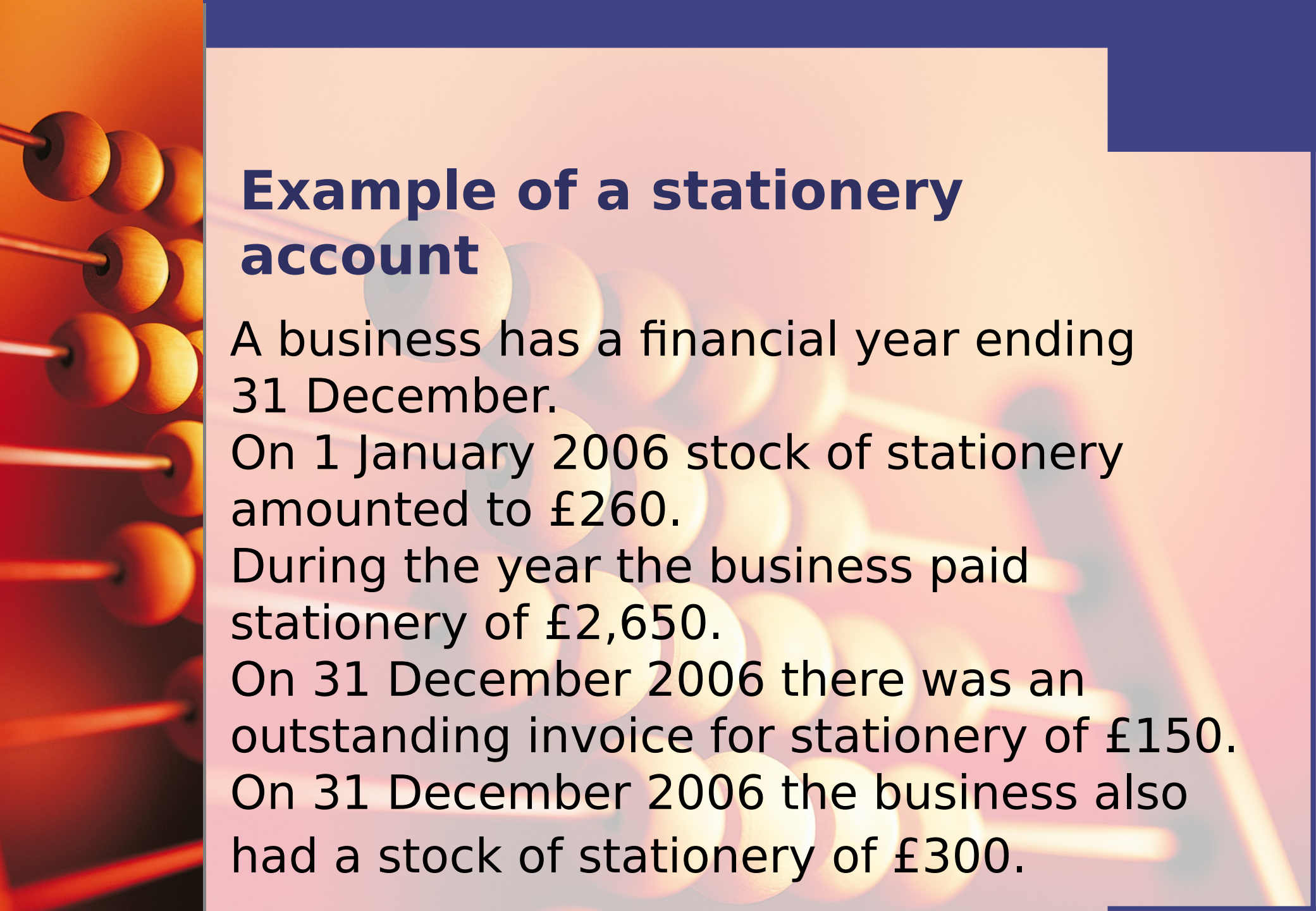
**Profit and loss account for the year ended
31 December 2006 (extract)**

Gross profit	xxx	
Add rent received		2,350

**Balance sheet as at 31 December 2006
(extract)**

Current liabilities

Prepaid rent receivable	500
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Example of a stationery account

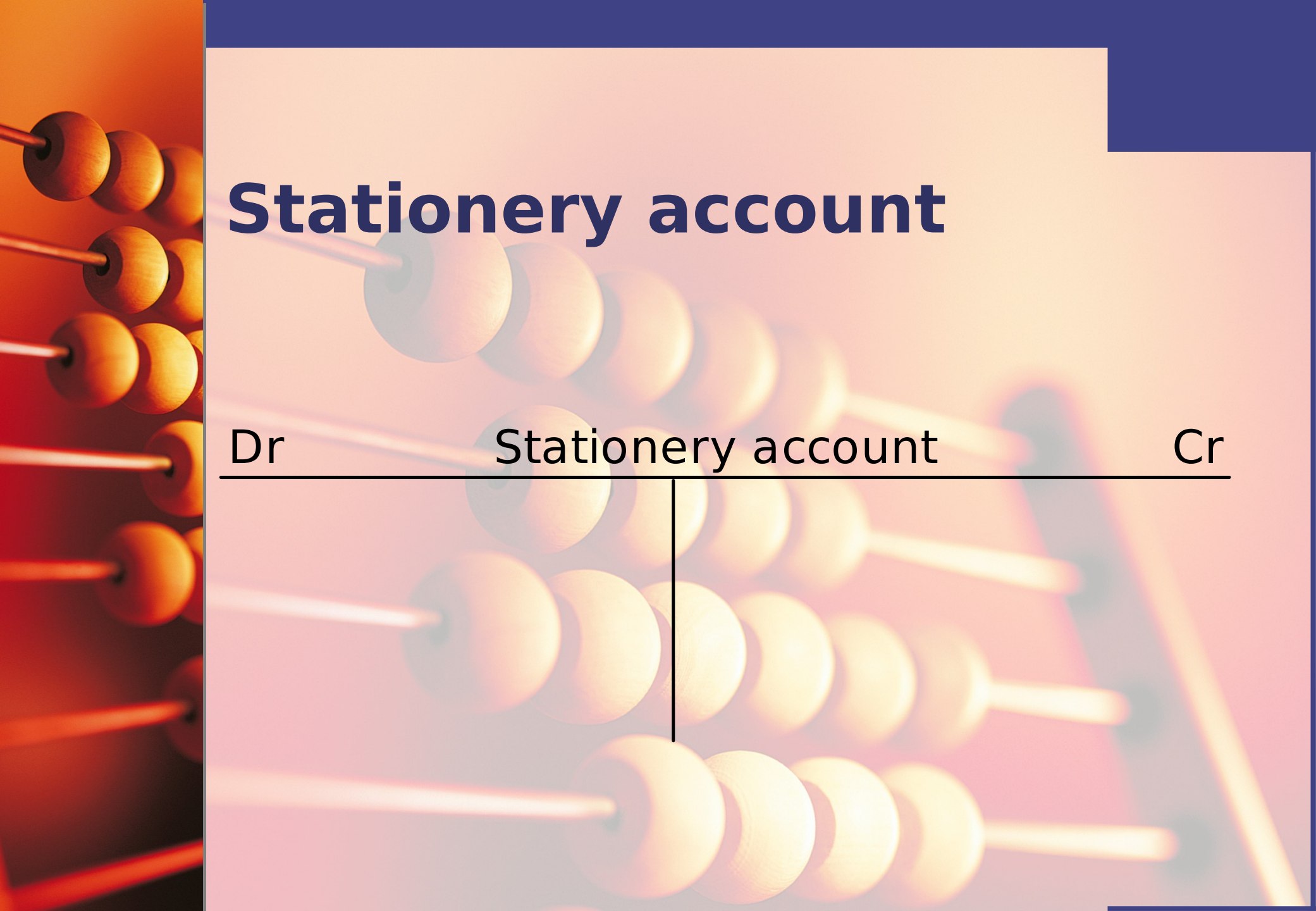
A business has a financial year ending 31 December.

On 1 January 2006 stock of stationery amounted to £260.

During the year the business paid stationery of £2,650.

On 31 December 2006 there was an outstanding invoice for stationery of £150.

On 31 December 2006 the business also had a stock of stationery of £300.



Stationery account

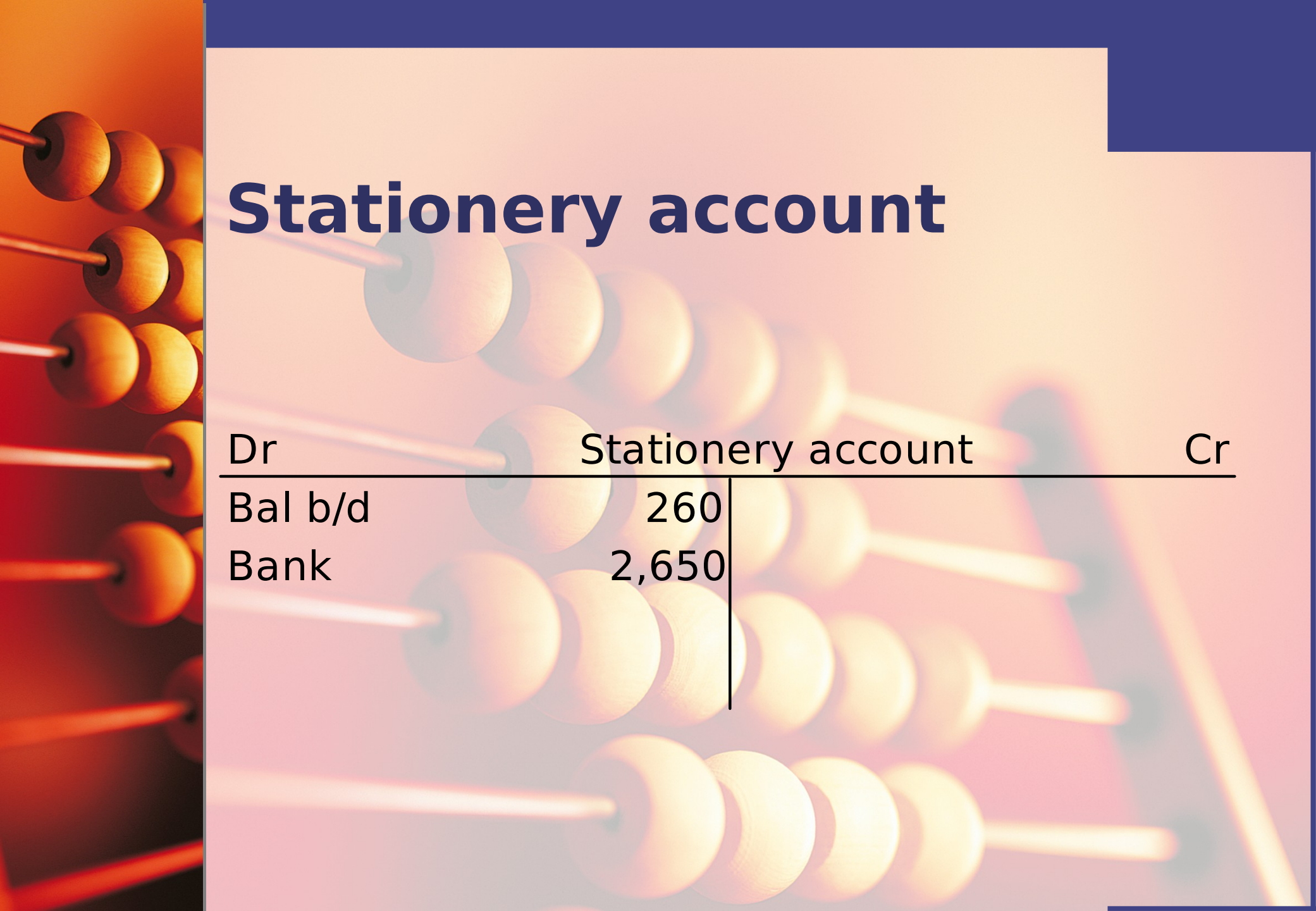
Dr

Stationery account

Cr

Stationery account

Dr	Stationery account	Cr
Bal b/d	260	



Stationery account

Dr	Stationery account	Cr
Bal b/d	260	
Bank	2,650	

Stationery account

Dr	Stationery account	Cr
Bal b/d	260	
Bank	2,650	
Bal c/d	150	Bal c/d 300
	<u> </u>	<u> </u>
	<u> </u>	<u> </u>

Stationery account

Dr	Stationery account		Cr
Bal b/d	260		
Bank	2,650	Profit and loss	2,760
Bal c/d	150	Bal c/d	300
	<u>3,060</u>		<u>3,060</u>

**Profit and loss account for the year ended
31 December 2006 (extract)**

Less expenses	
Stationery	2,760

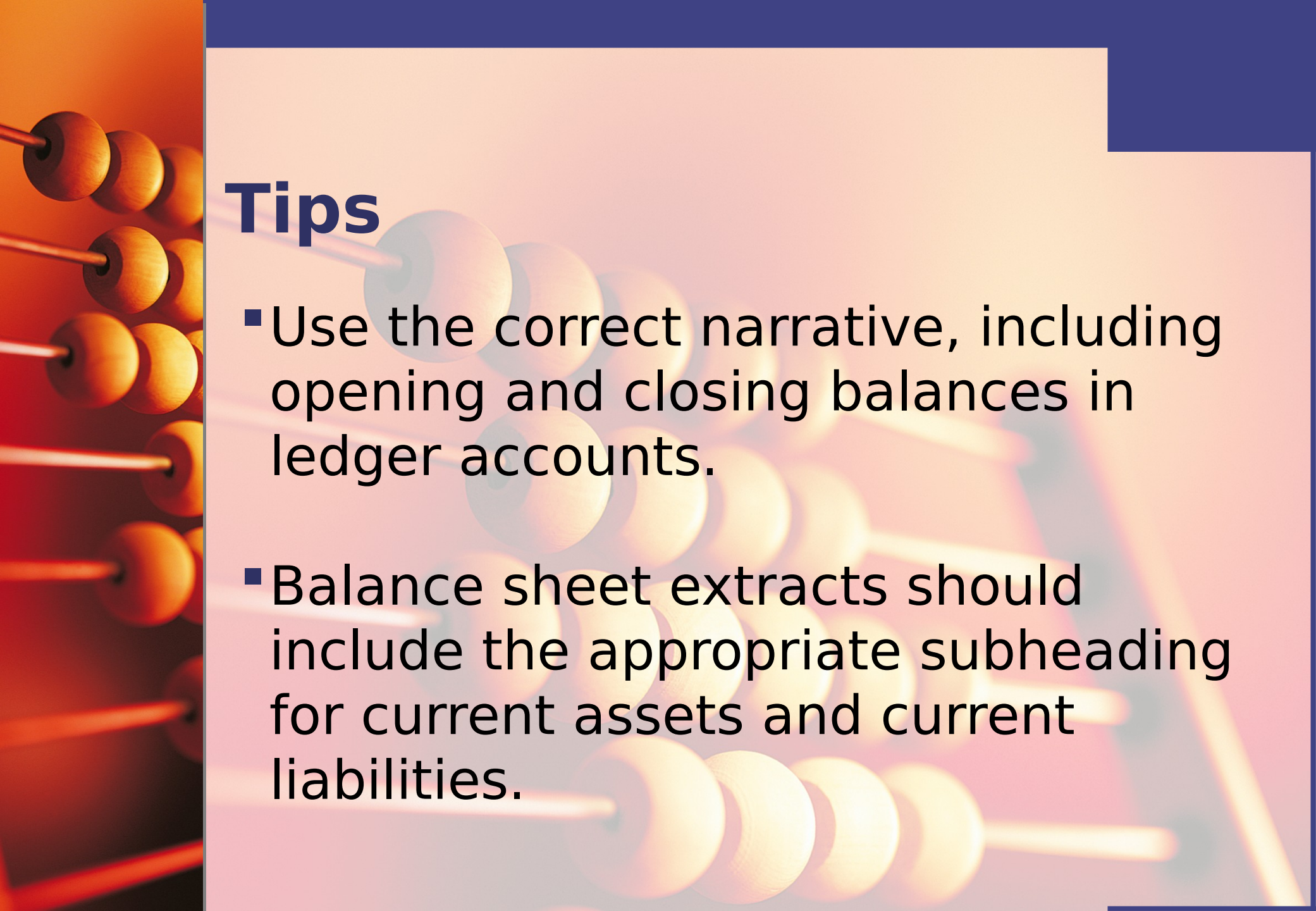
**Balance sheet as at 31 December 2006
(extract)**

Current assets

Prepaid stationery	300
--------------------	-----

Current liabilities

Accrued stationery	150
--------------------	-----



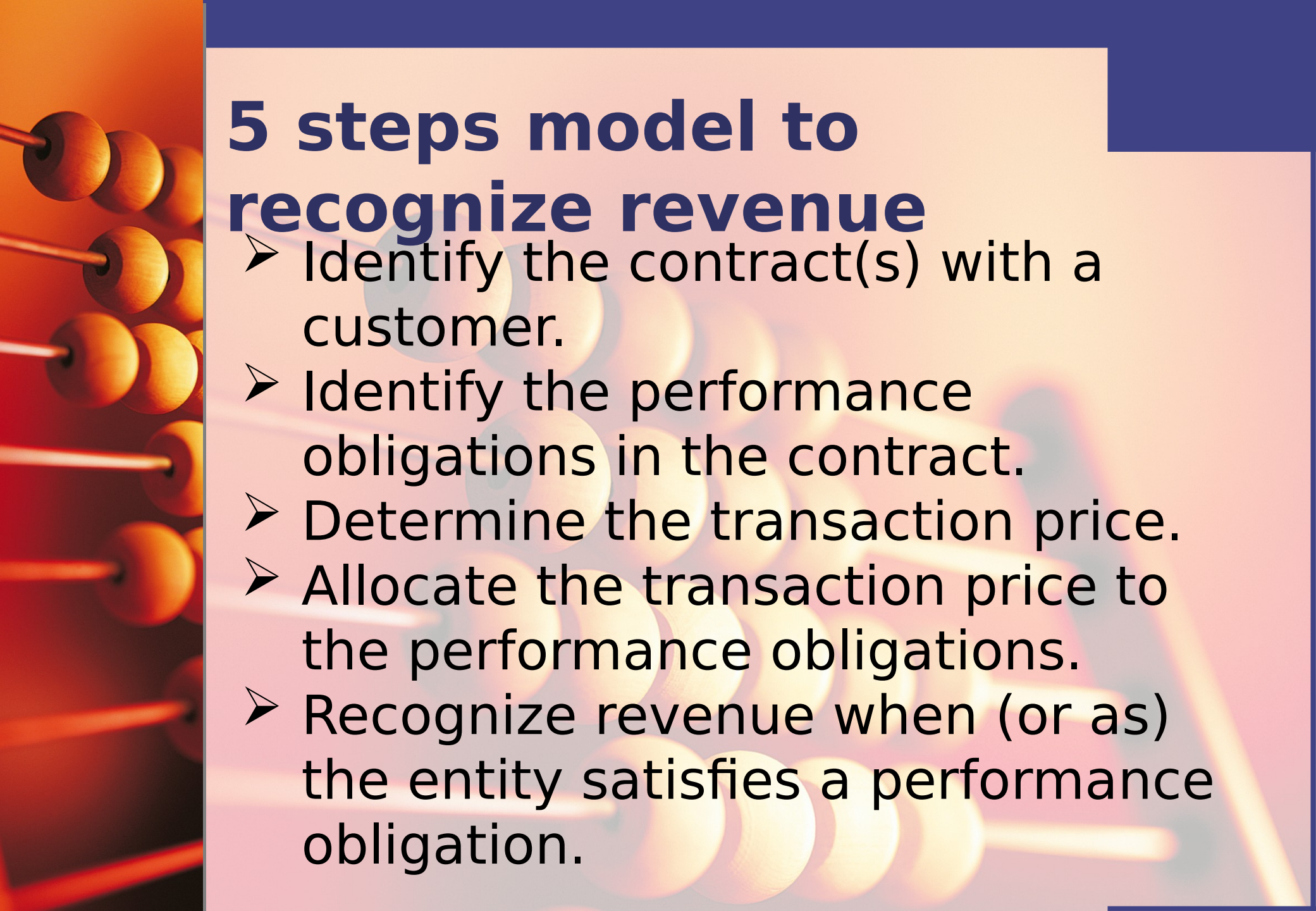
Tips

- Use the correct narrative, including opening and closing balances in ledger accounts.
- Balance sheet extracts should include the appropriate subheading for current assets and current liabilities.



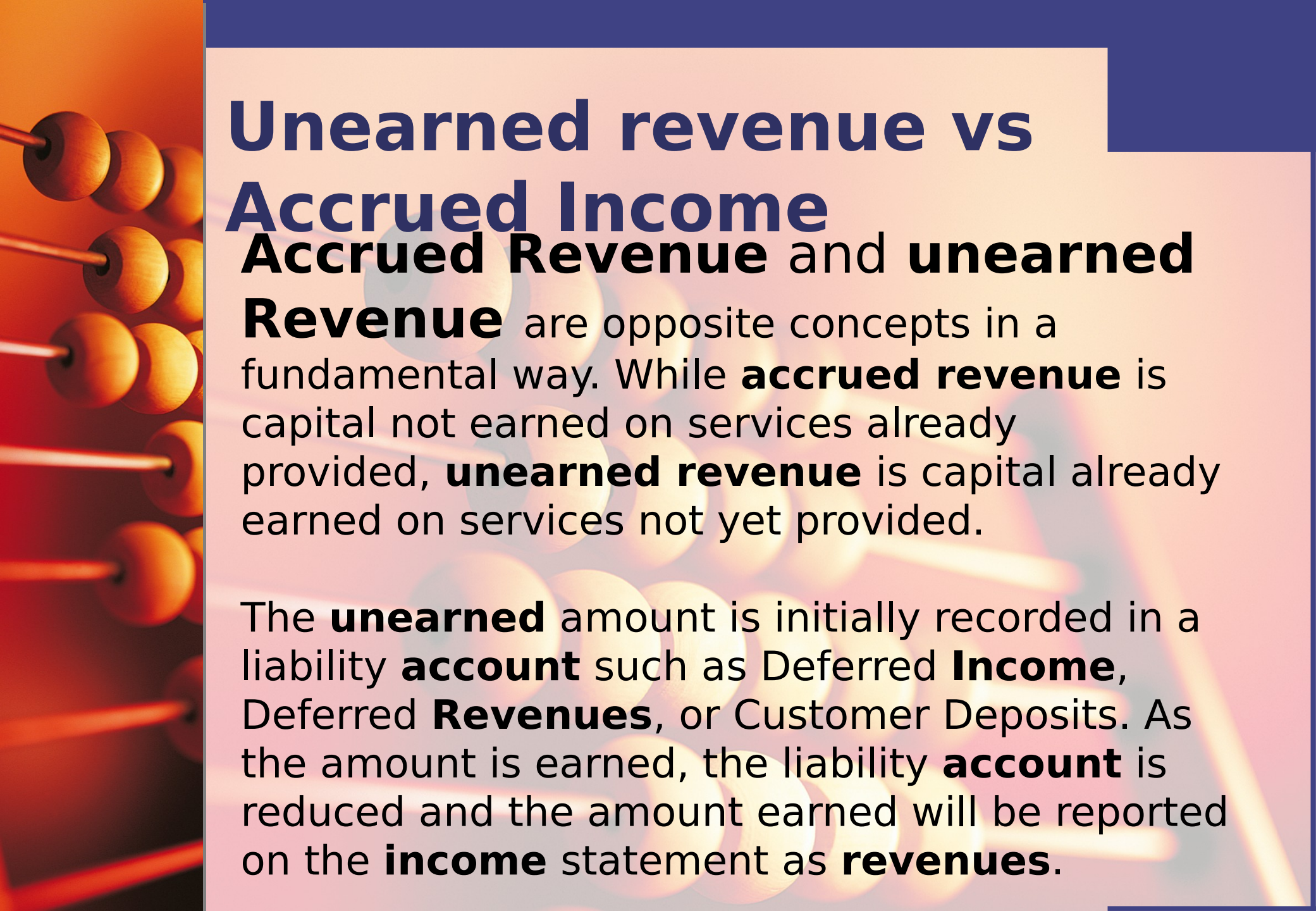
IFRS 15 Revenue Recognition

- ❑ IFRS 15 *Revenue from Contracts with Customers*, was issued on May 28, 2014
- ❑ The model addresses revenue arising from contracts with customers
 - ❑ The IASB and FASB created one comprehensive revenue recognition model for all contracts across virtually all entities and sectors.
 - ❑ New standard replaces virtually all existing IFRS and US GAAP guidance on revenue recognition



5 steps model to recognize revenue

- Identify the contract(s) with a customer.
- Identify the performance obligations in the contract.
- Determine the transaction price.
- Allocate the transaction price to the performance obligations.
- Recognize revenue when (or as) the entity satisfies a performance obligation.



Unearned revenue vs Accrued Income

Accrued Revenue and **unearned Revenue**

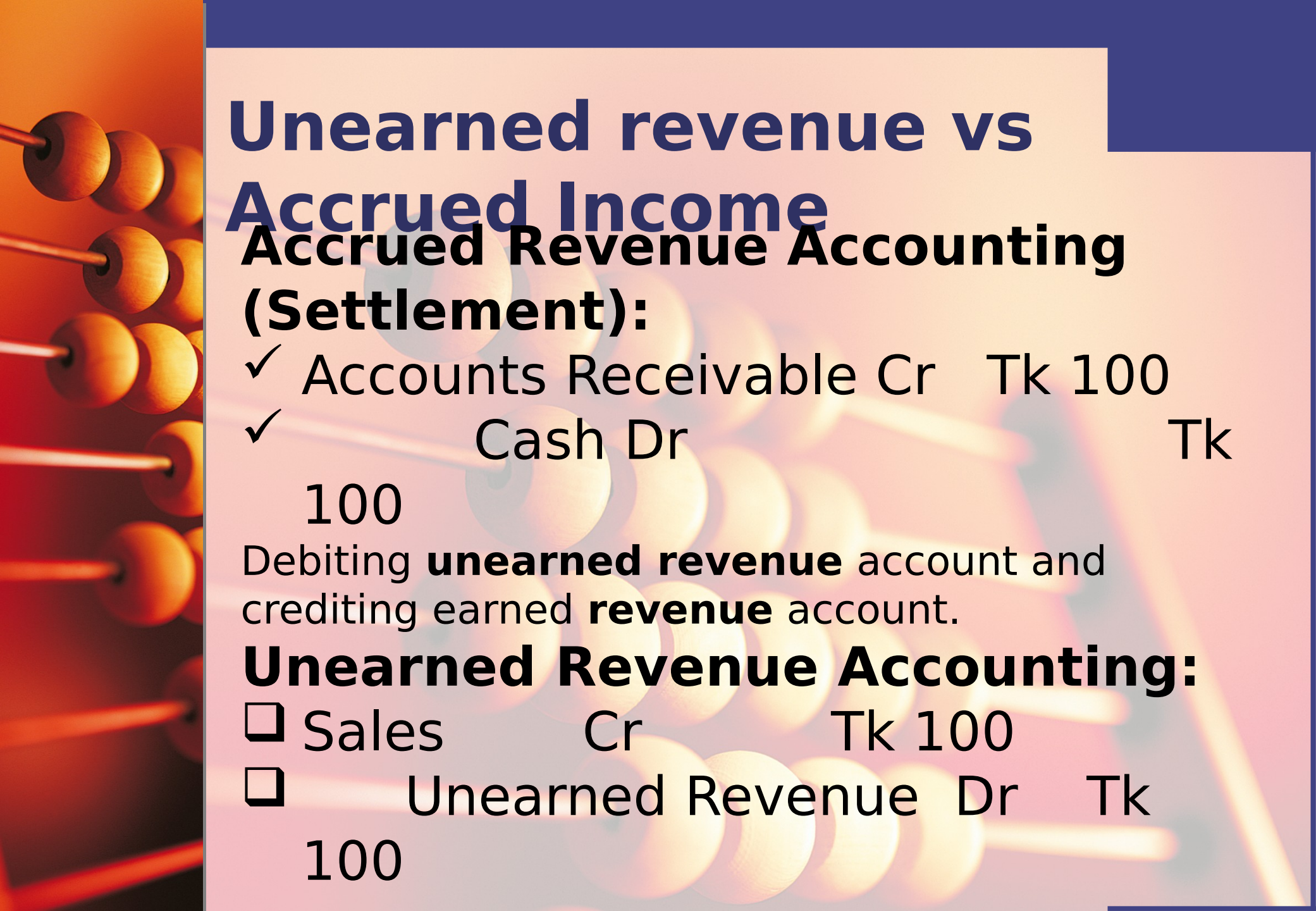
are opposite concepts in a fundamental way. While **accrued revenue** is capital not earned on services already provided, **unearned revenue** is capital already earned on services not yet provided.

The **unearned** amount is initially recorded in a liability **account** such as Deferred **Income**, Deferred **Revenues**, or Customer Deposits. As the amount is earned, the liability **account** is reduced and the amount earned will be reported on the **income** statement as **revenues**.

A vertical close-up photograph of an abacus. Several horizontal rods are visible, each with a round wooden bead. The beads are light brown with a visible wood grain. The background is a warm, solid orange color. The lighting is soft, creating a gentle gradient across the scene.

☐ Cash Dr Tk 100

☐ Unearned Revenue Cr Tk
100



Unearned revenue vs Accrued Income

Accrued Revenue Accounting (Settlement):

- ✓ Accounts Receivable Cr Tk 100
- ✓ Cash Dr Tk 100

Debiting **unearned revenue** account and crediting earned **revenue** account.

Unearned Revenue Accounting:

- ☐ Sales Cr Tk 100
- ☐ Unearned Revenue Dr Tk 100